

OPEN MEETING ITEM



0000020076

COMMISSIONERS  
JEFF HATCH-MILLER - Chairman  
WILLIAM A. MUNDELL  
MARC SPITZER  
MIKE GLEASON  
KRISTIN K. MAYES

ORIGINAL



ARIZONA CORPORATION COMMISSION

22

DATE: April 11, 2005

DOCKET NO: T-03654A-04-0910

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Teena Wolfe. The recommendation has been filed in the form of an Order on:

LEVEL 3 COMMUNICATIONS, LLC  
(ENCUMBER ASSETS)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

APRIL 20, 2005

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

MAY 3 AND 4, 2005

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250. For information about the Open Meeting, contact the Executive Secretary's Office at (602) 542-3931.

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BRIAN C. McNEIL  
EXECUTIVE SECRETARY

Arizona Corporation Commission

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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 JEFF HATCH-MILLER, Chairman  
4 WILLIAM A. MUNDELL  
5 MARC SPITZER  
6 MIKE GLEASON  
7 KRISTIN K. MAYES

8 IN THE MATTER OF THE APPLICATION OF  
9 LEVEL 3 COMMUNICATIONS, LLC FOR  
10 APPROVAL OF INCURRING DEBT AND  
11 FINANCING OBLIGATIONS.

DOCKET NO. T-03654A-04-0910

DECISION NO. \_\_\_\_\_

**ORDER**

9 Open Meeting  
10 May 3 and 4, 2005  
11 Phoenix, Arizona

12 **BY THE COMMISSION:**

13 On December 17, 2004, Level 3 Communications, LLC ("Level 3" or "Applicant") filed an  
14 application with the Arizona Corporation Commission ("Commission") requesting approval pursuant  
15 to A.R.S. § 40-285 to grant a security interest in its Arizona assets as part of financing arrangements  
16 involving its corporate parent, Level 3 Financing, Inc. ("Level 3 Financing").

17 On March 22, 2005, the Commission's Utilities Division Staff ("Staff") filed a Staff Report  
18 recommending approval of the application.

19 \* \* \* \* \*

20 Having considered the entire record herein and being fully advised in the premises, the  
21 Commission finds, concludes, and orders that:

22 **FINDINGS OF FACT**

23 1. Level 3 is a Delaware corporation and a wholly owned subsidiary of Level 3  
24 Financing, which is in turn a wholly-owned subsidiary of Level 3 Communications, Inc. ("Parent  
25 Company"). Level 3 is an authorized provider of intrastate telecommunications services in the State  
26 of Arizona and is authorized to provide telecommunications services nationwide.

27 2. In Decision No. 61737 (June 4, 1999), the Commission granted Level 3 a Certificate  
28 of Convenience and Necessity with authority to provide competitive resold and facilities-based local

1 exchange, exchange access, and interexchange telecommunications services in Arizona.

2 3. By its application in this proceeding, Applicant seeks approval to grant a security  
3 interest in its Arizona assets in connection with a refinancing. The Staff Report states that as of  
4 December 31, 2003, the book value of Level 3's assets in Arizona was \$122,438,153.

5 4. Level 3 provides service to 4 governmental entities and 329 business/wholesale  
6 customers in Arizona.

7 5. The application states that Applicant's parent, Level 3 Financing, has entered into a  
8 credit agreement whereby Applicant, upon obtaining regulatory approval, will pledge its assets and  
9 act as guarantor with respect to the credit agreement in the aggregate principal amount of up to \$850  
10 million.<sup>1</sup>

11 6. Level 3 states in its application that the proposed transactions will be transparent to  
12 consumers, will not cause a change in its officers or directors, and will not alter the rates, terms and  
13 conditions under which it currently provides service in Arizona.

14 7. The Staff Report describes the refinancing for which Level 3 requests authority to  
15 encumber its assets as follows: On December 2, 2004, Level 3 Financing completed purchase of  
16 \$1.105 billion principal of outstanding debt due in 2008. The purchase reduced amounts due in 2008  
17 to approximately \$1.3 billion, a 46 percent reduction in required debt service. Funding for the  
18 purchase was provided by new debt issues of \$1,075,000,000 that pushed the maturities of the  
19 amount purchased and reissued to 2011. The transaction further reduced annual cash interest expense  
20 by \$28 million, enhancing Level 3 Financing's ability to repay existing debt. As part of the credit  
21 package, Level 3 Financing offered for sale \$345 million of 5.25 percent convertible notes due in  
22 2011. Most of the proceeds of the note sales, along with \$730 million of funding from a senior  
23 secured loan, were used to complete the refinance. A portion of the proceeds of the sale of the notes  
24 was used to enter into bond hedge and warrant transactions related to Level 3 Financing's common  
25 stock. The \$345 million convertible debt can be exchanged at any time, subject to certain  
26 adjustments, for 251.004 shares of common stock per \$1,000 debt face value as long as the

27 \_\_\_\_\_  
28 <sup>1</sup> The initial proceeds received under the credit agreement will be approximately \$730 million, but the credit agreement allows for additional funds to be paid of up to \$850 million.

1 conversion takes place before December 15, 2011. The conversion rate equals to \$3.984 per share.

2 8. In its analysis of the application, Staff examined the consolidated financial statements  
3 of the Parent Company and its affiliates for September 30, 2004 taken from the Parent Company's  
4 Form 8-K. The consolidated entities had operating losses of \$381 million for the 9 month period  
5 ended September 30, 2004, which represents an improvement over the \$590 million loss in the  
6 similar period the previous year. Staff determined that the refinancing package did not alter the  
7 consolidated entities' capital structure,<sup>2</sup> and that the amount of debt outstanding also remains  
8 approximately the same.

9 9. Staff states that the consolidated entities' financial performance and capital structure  
10 would normally preclude authorization of the requested pledge of assets, but that since Level 3 has  
11 only governmental and business customers and there are many other sources for the services provided  
12 by Level 3, Level 3's customers would not be materially harmed by possible default on the loan  
13 facilities or the demise of Level 3's parent companies.

14 10. Staff states that authorization of the pledge of assets and guarantee in support of the  
15 financing transactions is warranted because the refinancing extends maturities on debt obligations,  
16 resulting in enhanced ability to repay existing debt. Staff states that the pledge of assets and  
17 guarantee will not impair Level 3's ability to provide telecommunications services in Arizona.

18 11. Staff recommends approval of Level 3's request for authorization to pledge its assets  
19 in support of loans in the amount of \$1,075,000,000 obtained by Level 3 Financing on the terms and  
20 conditions described in the application, and recommends approval of Level 3 granting liens in favor  
21 of the lender as required to secure the borrowings. Staff further recommends authorizing Level 3 to  
22 engage in any transaction and to execute any documents necessary to effectuate the authorization  
23 granted.

#### 24 CONCLUSIONS OF LAW

25 1. Level 3 is a public service corporation within the meaning of Article XV of the  
26 Arizona Constitution and A.R.S. § 40-285.

27  
28 <sup>2</sup> Staff notes that because the \$345 million debt package is convertible to common stock, the consolidated capital structure of the Parent Company and its affiliates could improve upon conversion.

2. The Commission has jurisdiction over Level 3 and the subject matter of the application.

3. Authorization of Level 3's pledge of assets and guarantee in support of Level 3 Financing's credit agreement is compatible with the public interest.

4. Staff's recommendations in Findings of Fact No. 11 are reasonable and should be adopted.

## ORDER

IT IS THEREFORE ORDERED that, pursuant to A.R.S. § 40-285, Level 3 Communications, LLC's application for approval to grant a security interest in its assets as set forth in its December 17, 2004 application is hereby granted.

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IT IS FURTHER ORDERED that Level 3 Communications, LLC is hereby authorized to engage in any transaction and to execute any documents necessary to effectuate the authorization granted.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER COMMISSIONER

COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this \_\_\_\_ day of \_\_\_\_\_, 2005.

BRIAN C. McNEIL  
EXECUTIVE SECRETARY

DISSENT \_\_\_\_\_

DISSENT \_\_\_\_\_

TW:mj

1 SERVICE LIST FOR:

LEVEL 3 COMMUNICATIONS, LLC

2 DOCKET NO.:

T-03654A-04-0910

3 Thomas H. Campbell  
4 Michael T. Hallam  
5 LEWIS AND ROCA  
6 40 N. Central Avenue  
7 Phoenix, AZ 85004  
8 Attorneys for Level 3 Communications, LLC

9 Richard M. Rindler  
10 Brian McDermott  
11 SWIDLER BERLIN SHEREFF FRIEDMAN, LLP  
12 3000 K. Street, NW, Ste. 300  
13 Washington, DC 20007

14 Neil Eckstein  
15 Senior Vice President and Assistant General Counsel  
16 Level 3 Communications, LLC  
17 1025 Eldorado Blvd.  
18 Broomfield, CO 80021

19 Christopher Kempley, Chief Counsel  
20 Legal Division  
21 ARIZONA CORPORATION COMMISSION  
22 1200 West Washington Street  
23 Phoenix, AZ 85007

24 Ernest G. Johnson, Director  
25 Utilities Division  
26 ARIZONA CORPORATION COMMISSION  
27 1200 West Washington Street  
28 Phoenix, AZ 85007